



UNITED STATES OFFICE OF PERSONNEL MANAGEMENT
Washington, DC 20415

The Director

March 1, 2007

The Honorable Richard B. Cheney
President of the Senate
United States Senate
Washington, DC 20510

Dear Mr. President:

The Office of Personnel Management (OPM) is submitting the enclosed legislative proposal, "To make improvements to the Civil Service Retirement System and the Federal Employees' Retirement System, and for other purposes." We request that it be referred to the appropriate committee for prompt and favorable consideration.

The draft bill would 1) clarify the long-standing policy that receipt of military retired pay bars civilian retirement service credit for all military service; 2) improve the provisions for computing Civil Service Retirement System (CSRS) annuities involving part-time service; 3) clarify the use of service as a cadet at a U.S. military academy for civilian retirement purposes; and 4) authorize Federal employees to invest bonuses in the Thrift Savings Plan.

First, the proposal clarifies the long-standing general policy that, unless another exception applies, receipt of military retired pay bars civilian retirement service credit for all military service. For military retirees under both CSRS and the Federal Employees' Retirement System (FERS) who do not waive their military retired pay, service credit is available only if the retirement is based on disability resulting from injuries that were incurred in combat or from an instrumentality of war during a period of war, or is under chapter 1223 of title 10, United States Code, or an earlier provision of law dealing with retirement of reservists (i.e., those who serve actively on weekends, summer drills, and when called to active service). This is based upon the public policy that, absent the expressly limited circumstances enumerated by the Congress, it is inappropriate to provide retirement credit under two Federal career retirement systems for the same periods of service.

A decision of the U.S. Court of Appeals for the Federal Circuit, *Babakitis v. OPM*, 978 F.2d 693 (Fed. Cir. 1992), created an anomalous exception to this general rule. It provided dual credit for a portion of the military service of certain individuals who retired on disability from the military, and who had breaks between periods of military service. By barring dual-credit only for the final period of military service for military disability retirees, the Court created an unwarranted anomaly in the otherwise consistent treatment of military service credit. Accordingly, this amendment would further the general policy against dual credits by stating that, when an

individual is retired from the military under circumstances other than those explicitly enumerated in the prior paragraph, no CSRS or FERS retirement credit will be available for any of the military service regardless of whether the military service was performed continuously, or over two or more separate periods.

Second, the measure addresses CSRS annuity computations involving part-time service. Under CSRS, an employee who has part-time service late in his or her career can experience an adverse effect in the computation of his or her annuity based on service performed before April 7, 1986. Current law for computing annuities involving part-time service resulted from the potential for abuse under the law as it existed prior to that date. While the current law is generally equitable, it can occasionally yield anomalous results when part-time service is involved in the computation of the "high-3"-year average salary. Further, it requires complex calculations that can lead to computational errors.

The draft bill would remedy this unfortunate situation, thus eliminating the potential adverse effect of part-time service performed late in an employee's career, and also would simplify the annuity computation in cases involving part-time service. Additionally, this proposal would change the computation on a prospective basis and only for those retiring after enactment.

Third, this measure addresses crediting cadet service at a U.S. military academy for civilian retirement. Specifically, this proposal would clarify the use of service as a cadet at a U.S. military academy for civilian retirement purposes. OPM (and the former Civil Service Commission) have consistently interpreted the term "military service" as including service as a cadet or midshipman at the Air Force, Army, Coast Guard, and Navy service academies. This measure is purely technical and is intended to confirm this long-standing interpretation, which was brought into question by an appeals court's decision in the case of *Horner v. Jeffrey*, 823 F.2d 1521 (Fed. Cir. 1986). This draft bill does not change the manner in which OPM currently computes annuities. Academy service would continue to be creditable in the same manner as other military service in the computation of annuities under the CSRS and FERS.

Finally, the draft bill would authorize Federal employees to invest bonuses in the Thrift Savings Plan (TSP) for Federal employees. Under now obsolete provisions, the Central Intelligence Agency was authorized to offer certain employees the opportunity to invest specified bonus money they received into the TSP, subject, of course, to the limitation under the Internal Revenue Code on the overall amount that may be invested in such a plan by an individual in a tax year. This proposal would provide similar authority on a permanent basis to all Federal employees. The measure would also specify that there would be no matching Government contribution for any bonus money so invested.

In summary, we believe enactment of this proposal will make needed technical improvements to the Civil Service Retirement System and the Federal Employees' Retirement System.

The Honorable Richard B. Cheney

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The Office of Management and Budget advises that the submission of this proposal is in accord with the program of the President.

A similar letter is being sent to the Speaker of the House of Representatives.

Sincerely,



Linda M. Springer
Director

Enclosures



UNITED STATES OFFICE OF PERSONNEL MANAGEMENT
Washington, DC 20415

The Director

March 1, 2007

The Honorable Nancy Pelosi
Speaker of the House
U.S. House of Representatives
Washington, DC 20515

Dear Madame Speaker:

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In summary, we believe enactment of this proposal will make needed technical improvements to the Civil Service Retirement System and the Federal Employees' Retirement System.

The Honorable Nancy Pelosi

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A similar letter is being sent to the President of the Senate.

Sincerely,

A handwritten signature in blue ink, appearing to read 'LMS', with a long, sweeping horizontal line extending to the right.

Linda M. Springer
Director

Enclosures

A BILL

To make improvements to the Civil Service Retirement System and the Federal Employees' Retirement System, and for other purposes.

Be it enacted by the Senate and the House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE

This Act may be cited as the "Federal Retirement Improvements Act of 2007".

SECTION 2. MILITARY RETIREES

(a) Section 8332(c)(2) of title 5, United States Code, is amended by striking "such" and inserting "that or any other".

(b) Section 8411(c)(2) of title 5, United States Code, is amended by striking "such" and inserting "that or any other".

SECTION 3. CIVIL SERVICE RETIREMENT SYSTEM COMPUTATION FOR PART-TIME SERVICE

(a) Section 8339(p) of title 5, United States Code, is amended by adding at the end the following new paragraph:

"(3) In the administration of paragraph (1)–

"(A) subparagraph (A) of such paragraph shall apply to any service performed before, on, or after April 7, 1986;

"(B) subparagraph (B) of such paragraph shall apply to all service performed on a part-time or full-time basis on or after April 7, 1986; and

"(C) any service performed on a part-time basis before April 7, 1986, shall be

credited as service performed on a full-time basis."

(b) The amendments made by this section shall take effect upon enactment of this Act, and shall apply only with respect to an annuity for which eligibility is based on a separation occurring on or after that date.

SECTION 4. RETIREMENT SERVICE CREDIT FOR CADET OR MIDSHIPMAN SERVICE

(a) Section 8331(13) of title 5, United States Code, is amended by striking "but" and inserting "and includes service as a cadet at the United States Military Academy, the United States Air Force Academy, or the United States Coast Guard Academy, or as a midshipman at the United States Naval Academy, but".

(b) Section 8401(31) of title 5, United States Code, is amended by striking "but" and inserting "and includes service as a cadet at the United States Military Academy, the United States Air Force Academy, or the United States Coast Guard Academy, or as a midshipman at the United States Naval Academy, but".

(c) The amendments made by this section shall apply to—

(1) any annuity, eligibility for which is based upon a separation occurring before, on, or after the date of enactment of this Act; and

(2) any period of service as a cadet or midshipman at the military service academy of the Army, Air Force, Coast Guard, or Navy, occurring before, on, or after the date of enactment of this Act.

SECTION 5. AUTHORIZING FEDERAL EMPLOYEES TO CONTRIBUTE BONUS PAY TO THRIFT SAVINGS PLAN ACCOUNTS

(a) Section 8351 of title 5, United States Code, is amended—

(1) by adding a new subsection (f) to read as follows:

“(f)(1) Under regulations prescribed by the Executive Director in consultation with the Director of the Office of Personnel Management, an employee making contributions to the Thrift Savings Fund out of basic pay may also make an advance election to contribute by direct transfer to the Thrift Savings Fund all or any part of any payment, other than basic pay, as may be prescribed by regulation.

“(2) For purposes of subsection (b)(2)(C), an amount transferred to the Thrift Savings Fund under paragraph (1) shall constitute basic pay.”; and

(2) in subsection (d) by—

(A) striking “(d)(1)” and inserting “(d)”; and

(B) repealing paragraph (2).

(b) Section 8432(k) of title 5, United States Code, is amended to read as follows—

“(k)(1) Under regulations prescribed by the Executive Director in consultation with the Director of the Office of Personnel Management, an employee making contributions to the Thrift Savings Fund out of basic pay may also make an advance election to contribute by direct transfer to the Thrift Savings Fund all or any part of any payment, other than basic pay, as may be prescribed by regulation.

“(2) For purposes of subsection (c), basic pay of an employee shall not include an amount transferred to the Thrift Savings Fund under paragraph (1).

“(3) For purposes of subsection (a)(3), an amount transferred to the Thrift Savings Fund under paragraph (1) shall constitute basic pay.”.

(c) The amendments made by this section shall take effect at the time prescribed in regulations issued by the Executive Director.

SECTION BY SECTION ANALYSIS

To accompany a draft bill

“To make improvements to the Civil Service Retirement System and the Federal Employees’ Retirement System, and for other purposes.”

SECTION 1. SHORT TITLE

The first section would provide that the bill may be cited as the “Federal Retirement Improvements Act of 2007”.

SECTION 2. MILITARY RETIREES

Section 2 would amend sections 8332(c)(2) and 8411(c)(2) of title 5, United States Code, by striking “such” and inserting “that or any other”. These amendments would further the long-standing general policy that, unless another exception applies, receipt of military retired pay bars civilian retirement service credit for all military service.

For military retirees under both the Civil Service Retirement System (CSRS) and the Federal Employees’ Retirement System (FERS) who do not waive their military retired pay, service credit is available only if the retirement is based on disability resulting from injuries that were incurred in combat or from an instrumentality of war during a period of war, or is under chapter 1223 of title 10, or any earlier provision of law dealing with retirement of reservists (i.e., those who serve actively on weekends, summer drills, and when called to active service). This is based upon the public policy that, absent the expressly limited circumstances enumerated by the Congress, it is inappropriate to provide retirement credit under two Federal career retirement systems for the same periods of service.

A court decision (*Babakitis v. Office of Personnel Management*, 978 F.2d 693 (Fed. Cir. 1992)) created an anomalous exception to this general rule. It provided dual credit for a portion of the military service of certain individuals who retired on disability from the military, and who had breaks between periods of military service.

By barring dual credit only for the final period of military service for military disability retirees, the court created an unwarranted anomaly in the otherwise consistent treatment of military service credit. Accordingly, this amendment would further the general policy against dual credits by stating that, when an individual is retired from the military under circumstances other than those enumerated above, no CSRS or FERS retirement credit will be available for any of the military service regardless of whether the military service was performed continuously, or over two or more separate periods.

SECTION 3. CIVIL SERVICE RETIREMENT SYSTEM COMPUTATION FOR PART-TIME SERVICE

Section 3 would amend the Civil Service Retirement law to simplify and rationalize the computation of annuities under the CSRS involving part-time service. The current provisions governing the computation of annuities involving part-time service have an unintended adverse effect on employees who perform part-time service at the end of their careers.

A CSRS annuity is computed based on an employee's "high-3" years' average salary, multiplied by a factor representing years of service. Before 1986, the high-3 average salary for employees who worked part-time was pro-rated based on the number of hours actually worked. Because an employee could switch to a full-time schedule in the last three years of service and thereby reap a benefit equal to that of an employee who worked full-time for an entire career, Congress decided in 1986 to reverse the computation formula. As a result, with service performed after April 6, 1986, the computation of part-time service is now based on a deemed full-time high-3 average salary, multiplied by the factor representing years of service. The resulting benefit is reduced by a fraction representing the actual time worked over the equivalent full-time service. Because this new computation applied only to service performed after April 6, 1986, the old formula continued to apply to service performed before that date. Consequently, if an employee with substantial full-time service before 1986 switches to a part-time schedule at the end of his or her career, the high-3 average salary that is applied to service before 1986 is the pro-rated salary or, if higher, the full-time salary from the years before the employee began working part-time. This results in a disproportionate reduction in the employee's benefit.

Section 3 of the bill would correct this anomaly by amending section 8339(p) of title 5, United States Code, to add a new paragraph (3) providing that, in the administration of paragraph (1), service performed before, on, or after April 7, 1986, shall be credited as service performed on a full-time basis. This would eliminate a disincentive for employees nearing the end of their careers who would like to phase into retirement by working part-time schedules, and would allow agencies to keep senior staff on board as part of a succession planning effort. This amendment also would provide a special annuity computation formula for employees who performed part-time service after April 6, 1986. For these employees, the proposed amendment would extend application of the full-time rates of pay in computing average salary to all service, regardless of when it was performed.

SECTION 4. RETIREMENT SERVICE CREDIT FOR CADET OR MIDSHIPMAN SERVICE

Section 4 would amend sections 8331 and 8401 of title 5, United States Code, to ratify the long-standing practice of the Office of Personnel Management (OPM) (and, previously, the Civil Service Commission) of granting service credit under CSRS and FERS for time spent as a cadet or midshipman at one of the military service academies.

OPM (and the former Civil Service Commission) have consistently interpreted the term "military service" as including service as a cadet or midshipman at the Air Force, Army, Coast Guard, and Navy service academies. This proposal is purely technical and is intended to confirm this long-standing interpretation, which was brought into question by an appeals court's decision in the case of *Horner v. Jeffrey*, 823 F.2nd 1521 (Fed. Cir. 1986).

SECTION 5. AUTHORIZING EMPLOYEES TO CONTRIBUTE BONUS PAY TO THRIFT SAVINGS PLAN ACCOUNTS

Section 6 would, effective at the time prescribed in regulations issued by the Executive Director of the Federal Retirement Thrift Investment Board in consultation with the Director of the Office of Personnel Management, amend sections 8351(d) and 8432 of title 5, United States Code, to permit Federal employees to contribute to their Thrift Savings Plan (TSP) accounts any payment, other than basic pay, as may be prescribed by regulation. In addition, it would repeal similar but more limited provisions that previously permitted certain Central Intelligence Agency employees to make direct payments to TSP under a now obsolete program.

Generally, under current law, Federal employees can only contribute basic pay to their Thrift Savings Plans, but not bonus or award monies. Authorizing such transfers will permit employees to take full advantage of their ability to contribute to their Thrift Savings Plans, consistent with existing limitations on the amount of contributions to certain retirement accounts. However, due to the operational complexities of such transfers, the amendment provides for the issuance of necessary regulations by the Executive Director.

In this regard, a major complexity is that there is often no advance notice of such payments to employees, thus necessitating that contingent elections need to be made in advance. Further, provisions need to be made so that employees are aware of the annual limits of the Internal Revenue Code, and can make their election in such a manner so as to avoid the problem of exhausting their annual transfer limit prematurely so as to lose potential agency matching payments under FERS.